Supreme Court of the United States

OCTOBER TERM, 1940

No. 465

In the Matter of
DEEP ROCK OIL CORPORATION, a corporation,
Debtor,

STANDARD GAS AND ELECTRIC COMPANY,
Petitioner,

vs.

JOHN M. TAYLOR, et al., as the Independent Committee for the Protection of the Holders of Preferred Stock of Deep Rock Oil Corporation; JOHN J. SHINNERS, et al., as a Reorganization Committee; H. N. GREIS, Trustee of Deep Rock Oil Corporation; SECURITIES AND EXCHANGE COMMISSION; and DEEP ROCK OIL CORPORATION,
Respondents.

BRIEF ON BEHALF OF THE INDEPENDENT COMMITTEE FOR THE PROTECTION OF THE HOLDERS OF PREFERRED STOCK, THE REORGANIZATION COMMITTEE, AND H. N. GREIS, TRUSTEE, IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

I.

INTRODUCTORY STATEMENT

Under date of February 27, 1939, this Court entered its opinion in this proceeding upon an extensive record and concluded that the District Court erred in approving a certain compromise of the claim of Standard Gas and Electric Company against its subsidiary Deep Rock Oil Corporation, the debtor herein, and the Plan of Reorganization based upon such compromise. In its opinion the Court discussed in detail the history of the relationship between Standard and Deep Rock and all of the items included in the Standard

claim and determined "the rights and the status of the preferred stockholders arising out of Standard's wrongful and injurious conduct in the mismanagement of Deep Rock's affairs." (306 U.S. 307, 322) The Court stated that an equity existed "after satisfaction of the creditors [Deep Rock noteholders] in which only the preferred stockholders and Standard can have an interest" and awarded to the preferred stockholders a "superior position" in that equity.

Later this Court in *Pepper* v. *Litton*, 60 S. Ct. 238, 246; 308 U.S. 295 (1939), characterized its holding in the instant case as follows:

> "In *Taylor* v. *Standard Gas and Electric Company*, 306 U.S. 307, this court held that the claim of Standard against its subsidiary (admittedly a claim due and owing) should be allowed to participate in the reorganization plan of the subsidiary only in subordination to the preferred stock of the subsidiary. This was based on the equities of the case—the history of spoliation, mismanagement and faithless stewardship of the affairs of the subsidiary by Standard to the detriment of the public investors."

The pending petition is an effort to relitigate in this Court the status and right of Standard to participate as a creditor in the reorganization of the debtor. Standard even asks that certain items in its claim be allowed on a parity with the notes. (Pet. pp. 34-37) The same supposed equities are urged which this Court has already repelled and the same claim is advanced which this Court has already subordinated.

As we shall show, the admitted maximum value of the debtor's assets is substantially less than the superior claims and interests of the holders of notes and preferred stock before taking into account any claim for Standard. The inescapable result is that Standard's claim, having been subordinated by this Court, has proven to be valueless and hence may not be given recognition in the reorganization.

II.

STATEMENT OF THE FACTS

Since the facts have been fully stated by the Circuit Court of Appeals for the Tenth Circuit (96 Fed. (2d) 693; 113 Fed. (2d) 266) and by this Court (306 U.S. 307), we shall not undertake a restatement and desire only to supply certain important omissions in the petition, as follows:

1. The District Court in the order of February 29, 1940, which gives rise to this proceeding, found that the fair value of the assets and properties of the debtor does not exceed $16,500,000. This finding of value shows no substantial change from the former maximum valuation of $17,000,000 which was approved by this Court. (306 U.S. 307, 314) Standard did not object below to the District Court's finding of value, nor does it challenge that determination by its petition herein.

2. The debt due the holders of the debtor's notes as of March 1, 1940 (after an interim distribution) was $13,000,000 and the interest of the preferred stockholders including dividends accrued to January 1, 1940, was $8,150,000, a total of $21,150,000, being $4,650,000 in excess of the conceded maximum value of the debtor's assets. Without including accrued dividends on the preferred stock, the debt due the holders of notes plus the par value of the preferred stock exceeds the conceded maximum value of the assets by $1,500,000.

3. The claim now advanced by Standard includes no items which were not in Standard's original claim as presented to this Court. (Rec. p. 1271) The record filed with the petition consists for the most part of the evidence in the record on the former appeal. The 1936 compromise of the Standard claim which this Court disapproved was based

on the allowance to Standard of its claims for net cash advances to Deep Rock or on its behalf and a portion of the advances made by Standard in connection with the acquisition and development by Deep Rock of the Bradstreet Acreage and Cracking Plant (the so-called Refining Company assets). (306 U.S. 307, 321) In its petition Standard not only seeks recognition in the reorganization for these cash items constituting the former compromise figure, but also renews its claims based on other items which were excluded in making the compromise. (Pet. p. 9)

4. Throughout the course of the litigation in the trial court, which has been in progress for over seven and one-half years, it has been uniformly claimed that the Refining Company assets belonged to the debtor and that this property, represented by the Refining Company stock, should be restored to Deep Rock free of any indebtedness to Standard. (306 U.S. 307, 320)

5. Prior to October 1, 1925 (the date of the Refining Company lease) Deep Rock was the owner of the stock of the Refining Company and the moneys expended for the acquisition and development of the Bradstreet Acreage and Cracking Plant were owed to Standard or its nominees. As of that date, but somewhat later, Standard undertook to change its position from that of creditor to that of proprietor and directed, through its chief accounting officer, the "sale" of the Refining Company stock to Standard in connection with the contemporaneous lease of the Refining Company assets to Deep Rock. (306 U.S. 307, 317-320) The order of the District Court recognized the invalidity of that transaction and restored the parties to their prior positions, leaving Standard as a creditor for the advances in question, as it was before October 1, 1925. (Rec. Vol. I, pp. 148-152, 159-161)

III.

ARGUMENT.

Summary of Argument.

A. The reasons advanced by petitioner for the allowance of the writ of certiorari are untenable.

B. The order of the District Court is the necessary consequence of the opinion and mandate of this Court in Taylor v. Standard Gas and Electric Company, 306 U. S. 307.

A. The reasons advanced by petitioner for the allowance of the writ of certiorari are untenable.

The petition suggests four reasons for the allowance of the writ (Pet. pp. 24-31), each of which we believe to be without merit for the following reasons:

1. No Injustice Has Been Done.

In support of the assertion that the order of the District Court is unjust Standard urges, first, the merit and equity of certain items in its claim (Pet. p. 25) and then suggests that the public holders of Deep Rock securities, which it characterizes as speculators, should not "profit" at the expense of the public security holders of Standard, who apparently are not considered to be speculators. Of course, both groups consist of members of the public who have from time to time acquired their respective securities by purchase on the open market at prevailing prices.

As to the first ground of alleged injustice:

The items in its claim upon which Standard relies are the same as those formerly presented to and reviewed by this Court. (Rec. p. 1271)

Standard filed its original proof of debt against Deep Rock on June 22, 1934, in the sum of $9,342,642.37 with in-

terest at 6% from February 28, 1933, which amount, as stated in the proof of debt, "is and represents the balance of accounts between Standard Gas and Electric Company and Deep Rock Oil Corporation for a period beginning June 1, 1919, and ending February 28, 1933." After the receipt by the District Court of the mandate of this Court subordinating the entire claim of Standard to the claims of the holders of Deep Rock notes and preferred stock, Standard, on December 28, 1939, filed its amended proof of debt in the sum of $6,129,248.36 covering the period from February 24, 1928* to February 28, 1933. This amended proof of debt did not include any item that had not been included in the original claim (Rec. p. 1271) and differed from the original claim in the following respects only:

(a) The amended claim as a matter of form covered only a portion of the period covered in the original claim, and

(b) There were omitted therefrom the large claims for rent on account of the Bradstreet Properties and Cracking Plant (the Refining Company assets) which had been included in the original claim.

The substance of these eliminated claims was renewed, however, by a petition filed by Standard on January 29, 1940, respecting the Refining Company assets. By this petition Standard sought by a new vehicle to establish its claims in connection with the Refining Company assets originally presented in the form of the claim for rent. (Pet. p. 42) The Refining Company petition states that the lease of the Refining Company assets was entered into "in an attempt to recover" Standard's expenditures in connection with the acquisition and development of such assets. (Rec. Vol. I, p. 119)

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*On this date the Standard claim on open account was balanced by the issuance of Deep Rock stock. (306 U.S. 307, 316)

The 1925 transfer of the Refining Company stock from Deep Rock to Standard, the issuance of the Refining Company note in the principal amount of $1,894,592.11 to Standard, and the contemporaneous lease of the Refining Company assets to Deep Rock were all dictated by Standard and parts of a single transaction. This endeavor by Standard to become the owner of the assets in question has been uniformly condemned by the courts. (96 Fed. (2d) 693, 698, 710; 306 U.S. 307, 318) The parties could only be restored to their positions prior to 1925 by requiring ownership to be returned to Deep Rock and remitting Standard to its position as creditor for the amount of its advances. The mere disaffirmance of the lease, which Standard concedes to be proper (Pet. pp. 42, 65), would be ineffective if Standard's claim to ownership is sustained.

In its former opinion this Court emphasized the Refining Company transactions as illustrating Standard's abuse of its position of domination over Deep Rock. Certainly these very transactions cannot result in giving Standard a valid claim which is immune from the subordination decree, and which Standard can enforce as a condition of the debtor's recovery of the Refining Company assets, which were originally purchased by Deep Rock and acquired for its use and benefit.

All items of the claim of Standard including its claims for reimbursement in connection with the Refining Company assets were before this Court and subordinated by the earlier opinion in this case. Indeed, a substantial portion of the advances made in connection with the Refining Company assets was included in the 1936 compromise allowance which this Court disapproved. (306 U. S. 307, 321) The compromise also provided for the return to Deep Rock of these assets. (306 U. S. 307, 321) We believe that this Court has clearly held, in disapproving the comprom-

ise, that Standard can participate for its various claims including those arising in connection with the Refining Company transactions, only in subordination to the holders of notes and preferred stock.

As to the second ground of alleged injustice:

It is suggested that the allowance to the noteholders and preferred stockholders of priority for the full amount of their claims and interests is an injustice. Standard throughout its petition repeatedly refers to the circumstance that certain of the present holders of notes and preferred stock have acquired such securities at depressed market prices. The only purpose of such statements must be the implicit suggestion that such holders should not be granted satisfaction of their claims in full. (Pet. p. 63) No authority is cited in support of this position.

Standard cannot be heard to contend that its subordinated claim has value on the ground that the claims of other creditors and preferred stockholders should be computed at less than the full face amount. The assignee of a claim is entitled to assert his claim for the full amount irrespective of the consideration which he may have paid for it, in the absence of fraud, actual or constructive.* There is no

**Security-First National Bank of Los Angeles* v. *Rindge Land and Navigation Co.*, 85 Fed. (2d) 557 (C. C. A. 9th, 1936); rehrg. den. 86 Fed. (2d) 3 (1936); cert. den. 299 U. S. 613 (1937); rehrg. den. 300 U. S. 686 (1937).

Texas Hotel Securities Corporation v. *Waco Development Co.*, 87 Fed. (2d) 395 (C. C. A. 5th, 1936); cert. den. 300 U. S. 679 (1937); rehrg. den. 301 U. S. 713 (1937).

In re Utilities Power & Light Corporation, 29 F. Supp. 763, 770 (D. C. Ill. 1939), app. dis. 7 Cir. C. C. A. on March 9, 1940.

In re Radio-Keith-Orpheum Corporation, 106 Fed. (2d) 22, 27 (C. C. A. 2nd, 1939).

Cf. *In re Tennessee Publishing Co.*, 81 Fed. (2d) 463, 466 (C. C. A. 6th, 1936).

Cromwell v. *County of Sac*, 96 U. S. 51, 60 (1877).

Wade v. *Chicago, Springfield & St. Louis Ry. Co.*, 149 U. S. 327, 343 (1893).

authority to the contrary and none is suggested. The consequences of destroying the marketability of securities in a corporation undergoing reorganization would be disastrous.

Not only is Standard's suggestion devoid of support by the authorities, but it cannot stand the test of elementary fairness and equity. The law imposes no fiduciary obligation upon the public holders of Deep Rock securities who purchased at the market price. On the other hand, it was Standard which, through its domination of Deep Rock, directed the issuance of such securities to the public. Standard insists that it does not contest the enforceability of the debtor's obligations in full. (Pet. p. 44) Standard, however, does urge that it should not be subordinated to the full "extent" of the claims of the notes and preferred stock. (Pet. p. 43) Whatever may be the proper technical characterization of the contention, in substance it is an obvious attempt by Standard to repudiate for its own benefit the engagements of Deep Rock represented by its outstanding notes and preferred stock. The promise of Deep Rock to the holders of its notes is to pay principal and interest unpaid to the date of payment. The preferred stockholders' preference rights are correspondingly definite.

We are unable to find in the opinion any qualification by this Court of its determination that the claims and interests of Standard were subordinated to the preferred stock. It follows that the senior interests are entitled to be satisfied in full prior to participation by Standard. Since the assets are even insufficient to meet the debt due the holders of notes plus the par value of the preferred, participation for Standard cannot be permitted.

2. THE ORDER BELOW DOES NOT CONFLICT WITH THE DECISION OF THIS COURT.

In support of the assertion that the order of the District Court did not involve matters already determined by this Court, Standard is required to suggest what this Court did decide. The petition states in this connection (p. 27):

> "What this Court decided in the *Taylor* case had to do with the securities which Standard was to receive under a new plan of reorganization * * *. At no place in its opinion in the *Taylor* case did this Court talk of subordination of Standard or Standard's claim except in terms of an award to Standard of participation in a plan of reorganization * * *."

Such statements contain their own refutation. This Court first stated the requirement of equity that the rights and the status of the preferred stockholders arising out of Standard's misconduct must be recognized. This Court then directed that "equity requires the award to preferred stockholders of a superior position" after satisfaction of the creditors (the noteholders). Subsequently this Court stated in *Pepper* v. *Litton* that the claim of Standard should be allowed to participate only in subordination to the preferred stock. We, therefore, believe it to be clear that Standard's status was fixed as subordinate for all purposes of the proceeding and that this Court did consider and determine "the equities of Standard's position *vis-a-vis* the equities of the positions of preferred stockholders and note holders of Deep Rock." (Pet. p. 21) Certainly Standard's rank or order of participation under a plan can not differ from but merely reflects its status or rank of interest in the assets of the debtor.

The refusal of the District Court, in the light of the value of the debtor's assets and the consequent valueless character of the Standard claim, to determine the validity or

amount of that claim was also consistent with, and not at variance from the prior decision of this Court. Under the opinion of this Court in this case, as repeated in *Pepper* v. *Litton*, the decree of subordination was made on the assumption that the claim or a substantial part of it was "due and owing."

3. THERE HAS BEEN NO DEPARTURE FROM THE USUAL COURSE OF JUDICIAL PROCEEDINGS.

We know of no basis upon which Standard can justify the statement that it was denied due process in the courts below. For seven years Standard has presented by evidence before the Master and in the District Court and by oral and written argument in the District Court, the Circuit Court of Appeals and this Court its contentions respecting its claim and the Refining Company transactions. Since 1933 it has been advised of the Trustee's position that the Refining Company assets should be restored to Deep Rock free of any claim from Standard. This Court itself stated as follows:

> "The Trustee in Bankruptcy attacked this transaction as fraudulent and asserted Deep Rock's ownership of all the property represented by the Refining Company's stock free of any indebtedness to Standard in respect of it." (306 U. S. 307, 320.)

By their former appeal the respondent, Independent Preferred Stockholders' Committee, insisted that the entire Standard claim was invalid, including all of the items relating to the Refining Company transactions. Prior to the hearing on February 27, 1940, Standard had introduced the brief additional evidence it desired to offer respecting the Refining Company transactions. (Rec. Vol. II, p. 1307) Prior to that hearing the respondents by their answers to the Refining Company petition (filed January 29, 1940) had

reiterated their consistent position that the Refining Company assets should be restored to the ownership of Deep Rock. (Rec. Vol. I, pp. 137, 142, 144, 147)

For Standard now to suggest that there was no issue raised with respect to the restoration to Deep Rock of the Refining Company stock and the cancellation of the Refining Company note held by Standard can only be explained as an inadvertent and careless disregard of the record. The order of the District Court simply put into effect by proper mechanics the fundamental conclusion that Deep Rock was in equity the owner of the Refining Company assets.

It is suggested in the petition that Standard was denied a hearing on the merits by the Circuit Court of Appeals. (Pet. p. 3) This statement is entirely without foundation. The substance of the motions to dismiss and affirm upon which the Circuit Court of Appeals acted presented all of the meritorious issues in the case. (Rec. pp. 1362-1366; 1371) This was recognized by Standard, which urged by brief and oral argument in the Circuit Court of Appeals substantially the same contentions which it here presents. (Rec. pp. 1372-1378)

4. THERE IS NO IMPORTANT PUBLIC ISSUE INVOLVED.

This proceeding, which has been so long before the courts and which has already been determined in all essential respects by this Court, certainly does not now involve any questions of law of importance to the public as distinguished from the private litigants. *Layne & Bowler Corporation* v. *Western Well Works,* 261 U. S. 387, 393 (1923) We submit that Standard is merely seeking to retry the issues which have already been adjudicated adversely to it by this Court. Standard's continued effort by the instant petition will further delay the consummation of the reorganization of the debtor to the detriment of the public

security holders. If there ever was a case where the discretion of this Court should be exercised in assisting the lower courts and the parties to break the jam and at last achieve constructive results, it is here presented.

We fail to understand how the fact that Standard itself has been reorganized in bankruptcy and now has a new management can affect or change the consequences which this Court has decreed must follow the mismanagement which occurred during the period while the claim arose. (Pet. p. 31)

B. The order of the District Court is the necessary consequence of the opinion and mandate of this Court in Taylor v. Standard Gas and Electric Company, 306 U. S. 307.

We have shown above that the order of the District Court does not conflict with the former opinion of this Court. In addition, we submit that the order below was the necessary consequence of that opinion. When this Court subordinated Standard to the preferred stockholders it necessarily held that all of the legal consequences of such subordination would follow. Since the conceded value of the assets of the debtor is insufficient to satisfy the claims of the holders of notes and the interests of the preferred stockholders, nothing remains for Standard in its subordinated position.* If Standard were permitted to participate in a reorganization plan under such conditions, the decree of subordination would be nullified. If Standard were to receive securities for its worthless interest, value would thereby be taken and diverted from the senior classes. This

*Since Standard does not challenge the District Court's finding of value, there is no necessity to comment upon the discussion (Pet. pp. 49-51) respecting the fluctuating earnings of Deep Rock. Of course, earnings, past, present and prospective, are all elements given consideration in determining value.

would not be subordination. Subordination means participation after, and only after, prior claims have been satisfied in full.

Since the balance of value remaining "after satisfaction of the creditors" is not equal even to the par value of the preferred stock, it is obvious that a division (as suggested in the petition, page 43) of that balance between the preferred stockholders and Standard could not accord with equitable principles. Such a division would deprive the preferred stockholders of the "superior position" awarded them.

Case, et al., v. *Los Angeles Lumber Products Company,* 60 S. Ct. 1, 308 U. S. 106 (1939).

Railroad Company v. *Howard,* 7 Wallace 392 (1868).

Louisville Trust Company v. *Louisville, New Albany and Chicago Ry. Co.,* 174 U. S. 674 (1899).

Northern Pacific Ry. Co. v. *Boyd,* 228 U. S. 482 (1913).

Kansas City Terminal Ry. Co. v. *Central Union Trust Company of New York,* 271 U. S. 445 (1926).

Securities and Exchange Commission v. *U. S. Realty and Improvement Co.,* 60 S. Ct. 1044 (1940).

It need hardly be suggested that the applicability of the established principle of the *Boyd* case to bankruptcy reorganization proceedings should not be relaxed in favor of Standard, which occupies its subordinated position as the result of its own conduct, which this Court has found to be "wrongful and injurious." Since, as a matter of equity, the public holders of all junior securities representing no remaining equity or asset value cannot participate in any reorganization, then surely Standard, in the light of the record in this case and the facts as determined by this

Court, cannot be accorded different or better treatment. *In re 620 Church Street Building Corporation,* 299 U. S. 24 (1936).

Standard's loss was caused by the substantial reverses suffered by the debtor prior to the institution of this proceeding, which depleted its assets to a point where the equity of interests subordinate to preferred stockholders had ceased to exist. The decree here complained of leaves Standard neither richer nor poorer than it was theretofore. An equity cannot be created for Standard where none exists.

By a novel and unsound process of reasoning Standard undertakes to compute an equity for its subordinated position by urging the disallowance of interest on the unpaid debt due the holders of Deep Rock notes. (Pet. pp. 59-63) It would indeed be a curious result of this Court's finding that Standard mismanaged Deep Rock (and of the decree of subordination which followed) that the claim of the noteholders must be limited to the principal of their debt. Since Standard is subordinated to the preferred stock, it is, of course, subordinated to the notes, principal and interest.

Furthermore, the law is clear that interest must be paid in full on claims in the order of their priority. This principle is firmly established in the law of both equity and bankruptcy reorganizations. The rule that where a debtor is insolvent no interest on claims accrues during the pendency of receivership or bankruptcy proceedings clearly cannot apply where the claims are of different rank of priority.

American Iron Co. v. *Seaboard Air Line Ry.,* 233 U. S. 261, 266 (1914).

Board of Commissioners of Sweetwater County v. *Bernardin,* 74 Fed. (2d) 809, 815 (C. C. A. 10th, 1934), Cert. Den. 295 U. S. 731 (1935).

In re Barclay Park Corp., 90 Fed. (2d) 595, 597 (C. C. A. 2nd, 1937).

Spring Coal Co. v. *Keech*, 239 Fed. 48, 51 (C. C. A. 4th, 1916).

In re Wickwire Spencer Steel Co., 12 F. Supp. 528, 535 (D. C. N. Y., 1935).

Fletcher, Private Corporations, Vol. 16, Chap. 64, Sec. 7937, page 632.

The controlling and obvious principle is that since the preferred stockholders of the debtor are to participate in the reorganization the note holders must be satisfied in full, both principal and interest. *Case, et al.* v. *Los Angeles Lumber Products Company*, 60 S. Ct. 1, 308 U. S. 106 (1939).

CONCLUSION.

Standard has already been fully heard in the District Court, twice in the United States Circuit Court of Appeals and once in this Court. This Court has decreed that Standard must be subordinated to the holders of preferred stock. The District Court has found that interests subordinate to preferred stock have no value and Standard has acquiesced in that finding. When a case has been determined by this Court a litigant must of necessity be foreclosed from relitigating his cause.

We respectfully urge that the petition for certiorari should be denied.

Respectfully submitted,

JASON L. HONIGMAN,
TRAVIS I. MILSTEN,
MILTON J. MILLER,
Attorneys for John M. Taylor, et al.

SEMPLINER, DEWEY, STANTON & HONIGMAN,
Of Counsel.

WILLIAM P. SIDLEY,
JAMES F. OATES, JR.,
GEORGE W. BALL,
VALJEAN BIDDISON,
Attorneys for the Reorganization Committee.

SIDLEY, MCPHERSON, AUSTIN & BURGESS,
Of Counsel.

GEORGE S. RAMSEY,
VILLARD MARTIN,
GARRETT LOGAN,
Attorneys for H. N. Greis, Trustee of Deep Rock Oil Corporation.

RAMSEY, MARTIN & LOGAN,
Of Counsel.

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 465

STANDARD GAS AND ELECTRIC CO., PETITIONER

v.

JOHN M. TAYLOR ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION

The Securities and Exchange Commission, named in the petition as intervener, is participating in the reorganization proceeding with the approval of the District Judge, pursuant to the provisions of Sections 208 and 276 c(2) of Chapter X of the Bankruptcy Act, as amended, c. 575, 52 Stat. 894, 905 (11 U. S. C., Secs. 608, 676 c(2)).

OPINION BELOW

The opinion of the Circuit Court of Appeals for the Tenth Circuit (R. 1372–1378) is reported in

113 F. (2d) 266. The decree of the District Court (R. 159–161) and the findings of fact and conclusions of law on which it is based (R. 148–152) are not reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered June 29, 1940 (R. 1378). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the decree of the District Court requiring the subordination of petitioner's claims to the claims and interests of the noteholders and preferred stockholders of the debtor, with the consequent exclusion of petitioner from participation in the reorganization, complies with the mandate of this Court in *Taylor* v. *Standard Gas & Electric Co.*, 306 U. S. 307.

2. Whether the District Court in determining the status of petitioner's claims denied it procedural due process or deprived it of its property without due compensation.

STATEMENT

The present controversy arises in the same reorganization proceeding which was before this Court in *Taylor* v. *Standard Gas & Electric Co.*, 306 U. S. 307 (hereinafter referred to as the "Taylor" case). In that case this Court reversed a

decision of the United States Circuit Court of Appeals for the Tenth Circuit which had affirmed orders of the United States District Court for the Northern District of Oklahoma confirming a plan of reorganization for Deep Rock Oil Corporation. The plan had been predicated on a compromise of certain claims asserted as a creditor by Standard Gas & Electric Co. (hereinafter called "Standard"), the owner of substantially all of the common stock of the debtor. This Court disapproved the plan because of the participation accorded Standard, deciding that the abuses in the management of the debtor by Standard required that Standard's claim as a creditor be subordinated to the interests of the debtor's preferred stockholders. The facts upon which that decision was based were stated in detail in this Court's opinion and are therefore not repeated here.

The claims of the noteholders and preferred stockholders, to which Standard's claim was required to be subordinated, exceeded in amount the value of the debtor's assets.[1] Accordingly, the "Reorganization Committee" subsequently filed a new or amended plan of reorganization in which Standard's claim, for which no value remained, received no participation (R. 42–72). Shortly thereafter Standard filed an "amended" claim (R. 91) which involved no items not included in the claim before this Court in the *Taylor* case (R. 1271). It

[1] The valuation of the debtor's assets is unchallenged by Standard.

differed from the original claim in that it covered only the period from 1928, when the account between the debtor and Standard was balanced, to 1933, the inception of the reorganization proceedings, and excluded any reference to the so-called Bradstreet Properties and Cracking Plant.[2] Standard's claims with respect to these properties were asserted, however, in a petition (R. 117) filed by it on January 29, 1940, alleging ownership of the properties, through the Refining Company, and seeking both compensation for the use of such assets and the return of the assets or reimbursement of Standard's "investment" therein, with interest. Hearings were held on the claim and petition and evidence was introduced by Standard in support of its claim (R. 1184–1319; Pet. 16).

The District Court found as facts (R. 149–150) (1) that as of March 1, 1940, the debtor's obligations to its noteholders totalled $10,000,000 for principal and $3,000,000 for interest; (2) that the liquidation preference of the 50,000 shares of the debtor's preferred stock was $5,000,000 plus cumulative dividends totalling $3,150,000; and (3) that the value of the debtor's assets did not exceed $16,500,000.[3] The court found, further, that the Refin-

[2] The history of these properties (hereinafter called the "Refining Company's properties") and of Deep Rock Oil and Refining Company (hereinafter called the "Refining Company") is referred to in the *Taylor* case. 306 U. S. at 317–320.

[3] This amount corresponds to the maximum valuation of $17,000,000 accepted by this Court in the *Taylor* case, after giving effect to interim changes. 306 U. S. at 314.

ing Company's properties had been acquired by and for the debtor and belonged to it and that any claim Standard might have arising out of transactions concerning such properties and the Refining Company was that of a creditor having a claim for money against the debtor. Such claim was declared to be of identical character with all other claims of Standard against the debtor.

The District Court's conclusions of law were that (1) Standard's claims of whatever nature, including its claims with respect to the Refining Company's properties, were subordinate to the claims of the noteholders and the interests of the preferred stockholders; (2) that the amount of such prior claims exceeded the entire asset value of the debtor; and (3) hence, that Standard's claims were of no value and were not entitled to any participation in the reorganization (R. 150–251). The District Court also determined, as a matter of law, that the debtor was the owner of the stock and properties of the Refining Company (R. 151). Inasmuch as the court had found that Standard's claims in respect of the Refining Company's properties were claims only against the debtor, it followed that they were invalid as claims against the Refining Company. The court concluded, therefore, that the note of the Refining Company held by Standard[4] should be discharged

[4] This note had been issued by the Refining Company to evidence the assumption by it of the debtor's obligation to Standard for advances in connection with the original acqui-

and that Standard should deliver to the debtor the stock and note of the Refining Company and documents evidencing title to its assets (R. 151–152).[5] Since Standard's claims, including those with respect to the Refining Company's assets, were found to be entitled to no participation in the reorganization, the District Court made no finding as to the amount or validity of the claims.

A decree was entered in conformity with these findings of fact and conclusions of law (R. 159). From this decree Standard appealed to the Circuit Court of Appeals, which affirmed[6] the decree. This petition for writ of certiorari is sought to review the decision of the Circuit Court of Appeals.

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sition of the properties. This assumption was related to the transactions discussed in the *Taylor* case, whereby Standard purported to take over the stock of the Refining Company from the debtor in 1925. 306 U. S. at 317–320.

[5] In effect, the court declared invalid the original transactions by which Standard purported, as of October 1, 1925, to take over from the debtor the stock and assets of the Refining Company, and restored legal title to such stock and assets to the debtor, remitting Standard to its claim against the debtor in the amount which was cancelled by the bookkeeping entry of October 1, 1925, and any proper additions.

[6] The respondents, including this Commission, moved to dismiss the appeal below on the ground that, inasmuch as Standard's principal objection to the decree of the District Court was to that court's construction of this Court's mandate (see R. 164), and since only this Court had jurisdiction to construe the mandate, the Circuit Court of Appeals could not entertain the appeal. See *Ex parte First National Bank*, 207 U. S. 61; and *Texas and Pacific Railway Co.* v. *Anderson*, 149 U. S. 237. The Circuit Court of Appeals denied the

ARGUMENT

It is the position of the Securities and Exchange Commission that the District Court correctly construed the mandate of this Court, and that its decree excluding Standard from participation in the reorganization followed inevitably both from the requirement of subordination directed by this Court and from the application to the case of well-settled principles of law. With respect to this decree, Standard has been afforded every requirement of due process of law.

I

In the *Taylor* case this Court disapproved a plan of reorganization, in which Standard's claims as a creditor were compromised in the amount of $5,000,000, because of the participation accorded Standard's claim. In considering the plan which was based on the compromise this Court examined all of the claims of Standard and concluded, in view of Standard's abuses in the control and man-

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motion to dismiss but affirmed the District Court's decree on the motion of one of the respondents to dismiss or to affirm, in the alternative. While we call the Court's attention to this question of the jurisdiction of the Circuit Court of Appeals, we do not now urge this point. Whether or not the ruling of the Circuit Court of Appeals was correct, any error in denying the motion to dismiss was harmless, since we believe that the affirmance was based on a correct construction of this Court's mandate. If this Court should now reverse the Circuit Court of Appeals with directions to dismiss the appeal, the result would be only to delay the termination of these long-pending proceedings.

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agement of the debtor, that "Equity requires the award to preferred stockholders of a superior position in the reorganized company", and that "No plan ought to be approved which does not accord the preferred stockholders a right of participation in the equity in the Company's assets prior to that of Standard, and at least equal voice with Standard in the management" (306 U. S. at 323, 324). In *Pepper* v. *Litton,* 308 U. S. 295, this Court said (p. 308):

> In *Taylor* v. *Standard Gas & Electric Co.,* 306 U. S. 307, this Court held that the claim of Standard against its subsidiary (admittedly a claim due and owing) should be allowed to participate in the reorganization plan of the subsidiary only in subordination to the preferred stock of the subsidiary. This was based on the equities of the case—the history of spoliation, mismanagement, and faithless stewardship of the affairs of the subsidiary by Standard to the detriment of the public investors.

We believe it clear that the Court contemplated that Standard's claim was to be subordinated to the interests of the preferred stockholders and that the District Court correctly so held.

In view of the subordination required by this Court, and the finding of the District Court that the value of the debtor's assets is less than the amounts of the prior claims of the noteholders and preferred stockholders, the District Court necessarily concluded that Standard's claims were en-

titled to no participation in the reorganization. Any other conclusion would have failed to give full effect to the requirement of subordination of Standard's claims directed in the *Taylor* case, and would have been contrary to the controlling decisions of this Court in *Case* v. *Los Angeles Lumber Products Co., Ltd.*, 308 U. S. 106, and *In re 620 Church Street Bldg. Corp.*, 299 U. S. 24.

The arguments advanced in Standard's petition in opposition to these conclusions are insubstantial and do not warrant review by this Court.

1. Standard contends that its claims are valid and meritorious and entitled to participation for the greater part, if not entirely, on a parity with the claims of the noteholders. These claims, it is stated (Pet. Brief 35–36, 52–58), include net cash advances, part of which were used by the debtor and part paid to the security holders of the debtor as interest and dividends; interest on Standard's loans to the debtor; interest on securities of the debtor held by Standard; Standard's "investment" in the Refining Company's assets and compensation for the use thereof by the debtor; and claims for services rendered by the affiliated management corporation. Standard's claims for cash advanced to the public security holders and for its "investment" in the Refining Company's assets are stated to be especially entitled to participation (Pet. 25, Brief 35, 51, 53). It urges further that its claims for dividends declared but unpaid on the

preferred and common stocks held by Standard are entitled at least to a position of seniority to the preferred stockholders' claims.

These items were all in the account considered and required to be subordinated in the *Taylor* case (R. 1271). In its opinion (pp. 311–312), this Court stated that the claim before it included "Cash payments by Standard to Deep Rock, or to others for its account, as shown by the books"; "Management and supervision fees paid or credited to Management Corporation"; "Interest charges by Standard to Deep Rock on open account balances"; "Rental charges upon a lease to Deep Rock of oil properties owned by a Standard subsidiary but claimed by petitioners to belong, in equity, to Deep Rock"; "Debits by Standard to Deep Rock of the amounts of dividends declared by Deep Rock to Standard, but not paid"; and "hundreds of debits and credits representing other intercompany items." The claim with respect to the Refining Company's assets was discussed by the Court at length (pp. 317–320). The fact that the claim included advances for payment of dividends to outsiders was mentioned (pp. 316–317). In its opinion this Court also pointed out (pp. 321–322) Standard's contention that, eliminating from the account dividends, management fees and all other questionable items, net cash advances since 1928 (when the present "amended claim" begins) plus the claims relative to the Refining Company's properties equalled the compromise figure, and that

at least as to such amount, there could be no criticism of the recognition of Standard's claim (pp. 321–322). Notwithstanding this contention by Standard, the entire claim was required to be subordinated.

No new matter has now been introduced. Standard's claim is the same as before. As to the validity of the claim, Standard's contentions are unimportant. In view of the debtor's valuation and the amount of senior claims, Standard's subordinated claim is necessarily without value in fact, whatever the amount at which it might be established.

2. Standard also contends that it is inequitable to subordinate its claims to the interests of the preferred stockholders. It asserts first that it has not violated its fiduciary duty; that there is no evidence in the record of mismanagement by Standard, or of damage to debtor's security holders as a result of any act or omission of Standard, or of any benefit to Standard from its relationship with the debtor. This is manifestly an attempt to relitigate the *Taylor* case, where this Court determined each of these issues.

Standard urges further not only that its claim is meritorious but that it would be particularly inequitable to subordinate it because of the nature of the claims of some of the debtor's public security holders. Standard contends that many noteholders and preferred stockholders of the debtor acquired their securities on the market at substan-

tial discounts and that they would receive a windfall [7] if they were permitted to participate in the reorganization for the full amount of their claims. Since any participation by Standard would be at the expense of the public claimants, the "windfall" argument is an attempt to reduce the senior claims in order to impart value to Standard's subordinated claim. This argument of Standard is without merit or authority. The assignee of a claim is entitled to assert it for the full amount, regardless of the price paid,[8] unless there is fraud. Standard has neither alleged nor established fraud. The adoption of the principle urged by Standard would destroy the marketability of the securities

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[7] Standard assumes that large profits will accrue to the security holders under the plan confirmed by the District Court. See, however, the advisory report of the Securities and Exchange Commission on the value and prospects of the debtor. S. E. C. Corporate Reorganization Release No. 23, April 26, 1940.

[8] *Security-First National Bank of Los Angeles* v. *Rindge Land & Navigation Co.*, 85 F. (2d) 557 (C. C. A. 9th, 1936), rehrg. denied, 86 F. (2d) 3, certiorari denied, 299 U. S. 613, rehrg. denied, 300 U. S. 686; *Texas Hotel Securities Corporation* v. *Waco Development Co.*, 87 F. (2d) 395 (C. C. A. 5th), certiorari denied, 300 U. S. 679, rehrg. denied, 301 U. S. 713; *In re Utilities Power & Light Corporation*, 29 F. Supp. 763, 770 (N. D. Ill.), app. dism., C. C. A. 7th, on March 9, 1940; *In re Radio-Keith-Orpheum Corporation*, 106 F. (2d) 22, 27 (C. C. A. 2d). Cf. *In re Tennesseee Publishing Co.*, 81 F. (2d) 463, 466 (C. C. A. 6th), aff'd, 299 U. S. 18; *Cromwell* v. *County of Sac*, 96 U. S. 51, 60; and *Wade* v. *Chicago, Springfield & St. Louis R. R. Co.*, 149 U. S. 327, 343.

of corporations in reorganization. Furthermore, Standard has no equities against the bona fide purchasers of the debtor's securities to justify a disregard of their contractual rights.

Standard urges, further, that its claims should not be excluded from the reorganization because the debtor's properties and business are speculative in nature. The speculative nature of the enterprise, however, was necessarily an element involved in the valuation to which Standard has not objected. Its present contention is merely an attempt to justify its participation in the reorganization despite the absence of value for its claims.

3. Standard denies that the lower courts' interpretation of the opinion of this Court was correct (Pet. 25 and 27). In order to reassert its claims on a parity with those of the noteholders, it contends that "the *Taylor* case dealt with a voluntary, agreed-upon reorganization, whereas the order now appealed from is one of complete bar and foreclosure against Standard" (Pet. 25); that this Court in the *Taylor* case did not "talk of subordination" of Standard's claims except in terms of award to Standard of participation in a plan of reorganization (Pet. 27–28) and that the securities thus to be received by Standard were to represent voting rights not greater than those allotted to the preferred stockholders; that "it is clear too that this Court's opinion assumed that the parties

would ultimately agree on a new plan of reorganization, consistent with the opinion" but that such agreed-upon plan was found to be impossible (Pet. 27); and that "In the *Taylor* case, this Court did not, and on the record before it could not, decide the exact extent of the priorities of note holders and preferred stockholders over the claim of Standard as a creditor" (Brief 43). Standard then urges that it is entitled to a participation in a plan on a parity with the noteholders for the greater part, if not all, of the claim which it now advances (Pet. 25, 35–36; Brief 52–58).

If we correctly understand these contentions, they would interpret the opinion in a manner which would render the decision of this Court meaningless. Apparently Standard argues that this Court did not determine the status of Standard's claims except in relation to the participation which Standard could receive in a "voluntary, agreed-upon reorganization", and that, absent such an agreement, Standard is not to be subordinated to the preferred stockholders, but on the contrary is entitled to have its claims participate on a parity with the claims of the noteholders. Under that interpretation, Standard's claims would be subordinated to those of the preferred stockholders only upon, and to the extent of, its agreement, and Standard would control the adoption of a plan. Such an interpretation is obviously untenable.

4. Standard then argues that, assuming subordination, its claims are entitled to participate because the claims of the senior security holders do not exhaust the assets of the debtor. Its contention is that for the purpose of measuring the participation of the noteholders' and stockholders' claims in the plan of reorganization, interest on the notes and dividends on the preferred stock accrued after the commencement of the proceedings must be disregarded. It is unnecessary, however, to consider the matter of preferred stock dividends. After providing for the payment of the noteholders' claims for principal and interest, the value of the debtor's assets is insufficient to satisfy in full the claims of the preferred stockholders, exclusive of accrued dividends.

Standard's contention with respect to interest on the debtor's notes is based on the assumption that, adding its claim to that of the noteholders, the debtor is insolvent. The case is thus argued to come within the rule that interest will not be accrued in favor of the unsecured creditors of an insolvent corporation. But this argument ignores the subordination of Standard's claim to that of the preferred stockholders, and necessarily to that of the noteholders. Where, as in this case, the assets are sufficient to satisfy the claims of the noteholders in full, including interest, it is clear that, even in bankruptcy, such interests must be satisfied before junior security holders are permitted to participate. This Court in *American Iron and Steel*

Co. v. *Seaboard Air Line Ry.*, 233 U. S. 261, 266–267, said: [9]

> * * * in case funds are not sufficient to pay claims of equal dignity, the distribution is made only on the basis of the principal of the debt. But that rule did not prevent the running of interest during the Receivership; and if as a result of good fortune or good management, the estate proved sufficient to discharge the claims in full, interest as well as principal should be paid. Even in bankruptcy * * * it has been held, in the rare instances where the assets ultimately proved sufficient for the purpose, that creditors were entitled to interest accruing after adjudication. * * *
>
> The principle is not limited to cases of technical bankruptcy, where the assets ultimately prove sufficient to pay all debts in full but principal as well as interest, accruing during a receivership, is paid on debts of the highest dignity, even though what remains is not sufficient to pay claims of a lower rank in full. * * *

On the facts of this case, it is clear that the rule relied upon by Standard is inapplicable.

II

Standard contends (Pet. 30) that that portion of the decree of the District Court relating to the Re-

[9] See, also, *Board of Commissioners of Sweetwater County* v. *Bernardin*, 74 F. (2d) 809, 815 (C. C. A. 10th), certiorari denied, 295 U. S. 731; *In re Barclay Park Corporation*, 90 F. (2d) 595 (C. C. A. 2d).

fining Company's properties is unfair and involves a violation of substantive and procedural due process.

1. The transaction by which Standard purported to acquire the stock of the Refining Company was considered and condemned by this Court in the *Taylor* case.[10] Subsequently, when the issue of ownership of the property was raised in this proceeding, the District Court, in compliance with the obvious intention of this Court in the *Taylor* case, decreed the reversal of the transfer of October 1, 1925, and restored the parties to the positions they occupied before that transaction. The debtor was found to be the owner of the properties [11] and Standard was remitted to its remedies as a creditor on its original claim for advances.

Standard contends that the decree ordering the transfer of the note and stock and properties of the Refining Company to the debtor deprived Standard of its property without due compensa-

[10] 306 U. S. at pp. 317–318.

[11] In order to effectuate the decree, the District Court ordered Standard to surrender to the debtor certain title documents and the note and stock of the Refining Company. The note of the Refining Company was issued at the time of the original transfer, to evidence the assumption by the Refining Company of the debtor's obligation to Standard for advances as part of the purported consideration for the transfer. Inasmuch as the District Court, in effect, invalidated the transfer and restored Standard to its original position as a creditor of the debtor in respect of such advances, the note of the Refining Company evidencing the same advances was required to be cancelled.

tion. Its premise, however, is unsound. The property did not belong to Standard but to the debtor, and Standard has lost nothing except the fruits of an illegal transaction. It has not been deprived of its claim for the original advances, the only property to which it was entitled. Those advances, moreover, are merely part of its general claims, and their exclusion from participation in the reorganization, because the debtor's assets are insufficient in value to satisfy senior claims, is no deprivation of substantive due process of law. *In re 620 Church Street Bldg. Corp.*, 299 U. S. 24.

Standard's argument that, as a matter of equity, it is entitled to some compensation for the property is not supported by the cases upon which it relies. In those cases [12] the constructive trustee or wrongdoer improved or expended funds on the property while such property was in its possession, and compensation was allowed for the expenditures or improvements. In Standard's case, however, the original advances were made before the attempted transfer and gave rise only to a claim on open account. That claim, for whatever it was worth, was restored by the decree of the District Court. Standard added nothing to the Refining Company's properties after the illegal transaction,

[12] *Southern Pacific Company* v. *Bogert*, 250 U. S. 483; *Thomas* v. *Brownville, etc., R. Co.*, 109 U. S. 522; *McCandless* v. *Furlaud*, 296 U. S. 140, 167.

and the reversal of the transaction deprived it of nothing which it owned.

2. Standard contends, further (Pet. 30), that—

> In no pleading before the Court was an issue raised with respect to whether the note of the Refining Company held by Standard was valid or whether Standard should be directed to mark such note "paid", or whether Standard had received payment of such note; in no pleading before the Court was an issue raised as to whether Standard should be affirmatively ordered to transfer the stock of the Refining Company to the Debtor without receiving compensation. Standard was therefore denied notice and hearing, essential prerequisites of due process.

These contentions are wholly without merit. On January 29, 1940, Standard filed a petition asserting that the Refining Company was the owner of the Bradstreet Properties and Cracking Plant and that the stock of the Refining Company was owned by Standard. The petition requested the District Court to direct that the trustee in bankruptcy pay compensation to it for his use and occupancy of such properties, and that he surrender possession and control of such property or pay to Standard the amount of its "cash investment" in the Refining Company, with interest (R. 117–123). The respondents filed answers denying Standard's title to the properties and praying the court to de-

cree that the properties were beneficially owned by the debtor and to direct Standard to cause legal title to the properties to be conveyed to the trustee, or in the alternative to deliver to the trustee the capital stock of the Refining Company and its unpaid note held by Standard (R. 137–148).

These pleadings put in issue the title to the properties. The District Court had jurisdiction to decide that matter in a summary proceeding. The Refining Company's assets were in the possession and control of its trustee in bankruptcy;[13] and Standard itself had invoked that summary jurisdiction.[14] As an incident to that question of title, the pleadings put in issue the disposition of the stock and note of the Refining Company. The cancellation of the note and the return of the stock and note to the debtor were necessary incidents of the reversal of the original transaction of 1925 in which the note had been issued and the stock transferred to Standard.

On the issues thus raised Standard had its day in court. At the hearing on January 29, counsel for Standard introduced certain exhibits pertinent to its petition, including the record on Standard's claim before this Court in the *Taylor* case (R. 1262–1264, 1274; see Pet. 16). On January 30 he

[13] See *Thompson* v. *Magnolia Petroleum Co.*, 309 U. S. 478.

[14] See *James Talcott, Inc.* v. *Glavin*, 104 F. (2d) 851, 853 (C. C. A. 3d), certiorari denied, 308 U. S. 598.

introduced additional exhibits (R. 1275–1276), and apparently closed his case (R. 1307). Subsequently, respondents filed their answers to Standard's petition. The hearing was resumed on February 27 but Standard's counsel made no further attempt to introduce testimony (R. 1313–1319). The District Court had before it a full record on which Standard had ample opportunity to be heard.

CONCLUSION

Most of petitioner's contentions have already been decided by this Court. The decisions of the courts below were inevitable under the *Taylor* decision and raise no issues of importance. There is no conflict of decision. It is therefore respectfully submitted that the petition for a writ of certiorari should be denied.

FRANCIS BIDDLE,
Solicitor General.

CHESTER T. LANE,
General Counsel,
BERNARD D. CAHN,
HOMER KRIPKE,
IRVING S. ROGERS,
Attorneys,
Securities and Exchange Commission.

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